



**COUNCILMEMBER DONNA FRYE**  
City of San Diego  
Sixth District

**MEMORANDUM**

**DATE:** May 7, 2007

**TO:** Honorable Mayor and City Councilmembers

**FROM:** Councilmember Donna Frye *Donna Frye*

**SUBJECT:** 2003 Comprehensive Annual Financial Report (CAFR)

It is my understanding that there will be a request for a continuance of Item Number 201 (*Hearing on the City's Comprehensive Annual Financial Report for the Fiscal Year ending June 30, 2003*) on the May 7, 2007, City Council Docket to allow for further review by the City Council Audit Committee. In preparation for future discussion, I am providing the following information and recommendations.

**ISSUE:** Information that is pertinent to understanding and complying with the Kroll Remediations has been omitted from the Mayor's August 24, 2006 Memorandum to the City Council on the Kroll Report and from subsequent reports, the most recent of which is dated April 9, 2007 (Kroll Remediation Status Report Number 5).

On August 8, 2006, Kroll released their report. On page 248, it states that, "*A reputable independent auditing firm should be retained by the City's new Audit Committee which should, in connection with the annual audit of the financial statements of the City for the fiscal year ending June 30, 2008, conduct an audit of the City's internal controls, in accordance with the applicable auditing standards and issue a report thereon. Such report should, among other things, identify any material weaknesses and be included as part of the City's CAFR.*"

On August 24, 2006, Mayor Sanders issued a Memorandum to the City Council regarding his responses to the Kroll Report. The Kroll Remediations were assigned numbers and the above Kroll Remediation was assigned #36.

The last sentence for Kroll Remediation #36, "*Such report should, among other things, identify any material weaknesses and be included as part of the City's CAFR*" was somehow excluded from the Mayor's August 24, 2006 Memorandum and subsequent memos regarding Kroll Remediation #36.

**RECOMMENDATION:** Include the sentence, “*Such report should, among other things, identify any material weaknesses and be included as part of the City’s CAFR*” in all future references to Kroll Remediation #36, and provide updated information as to when this portion of Remediation #36 will be initiated/completed.

Page 248 of the Kroll Report states, “*The Mayor and the CFO should annually include in the City’s CAFR a signed management report on the financial statements and disclosures which shall include: (i) a statement of the City’s responsibility for establishing and maintaining an effective system of internal control over financial reporting and disclosures (ii) a statement setting forth the City’s assessment of the effectiveness of the internal controls as of the fiscal year-end, as well as identifying any material weaknesses in internal controls; (iii) a statement that, based on their knowledge, the CAFR does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the CAFR, in light of the statements made and circumstances under which they are made, not misleading with respect to the period covered, and (iv) a statement that this financial statement and other information included in the CAFR fairly present in all material respects the net assets and activities of the City for the period presented.*”

The above Kroll Remediation was assigned #58 in the Mayor’s August 24, 2006 Memorandum to City Council. The phrase, “*as well as identifying any material weaknesses in internal controls*” was somehow excluded from the Mayor’s August 24, 2006 Memorandum and subsequent memos regarding Kroll Remediation #58 (ii).

**RECOMMENDATION:** Include the phrase, “*as well as identifying any material weaknesses in internal controls*” in all future references to Kroll Remediation #58, and provide updated information as to when this portion of Remediation #58 will be initiated/completed.

**ISSUE:** There have been proposed modifications to the Kroll Remediation timeline that require clarification of managements’ responses (*Views of Responsible Officials*) to KPMG’s March, 2007 **Internal Control Report**. These changes to the timeline will push back the timely review of the City’s internal controls and other financial reporting issues.

On April 9, 2007, the Mayor issued a report to the City Council (Kroll Remediation Status Report Number 5, prepared for the April 23, 2007 Council Meeting). Status Report #5 included numerous timeline modifications to the implementation of the Kroll Report remediations as originally discussed in the August 24, 2006 Memorandum.

Regarding Kroll Remediations #36, #58 and #59, the Mayor’s Status Report Number 5 stated on page 13 that, “*Updated status relates to the areas of items 36, 58 and 59 that are underlined above. The audit of internal controls by an independent auditing firm is directly related to City management’s assessment of the effectiveness of internal controls. City management believes audit of the City’s internal controls by a reputable independent auditing firm should not take place until the City’s new Enterprise Resource*

*Planning (ERP) system has been implemented. By the time the ERP system is implemented, the City should be current on audits of its CAFRs and should have sufficient resources to focus on internal controls over financial reporting.”*

*“Additionally, the nature and structure of the City’s internal controls are anticipated to change (and be enhanced) as a result of ERP implementation. City management believes that documenting and assessing internal controls for the new ERP system will add significantly more value than documenting and assessing internal controls for the current accounting system that is more than 30 years old and is planned to be replaced in the near-term.”*

On April 19, 2007, City management officially issued its response to KPMG’s **Internal Control Report**. KPMG’s Recommendation, **Item 2003-1. Material Weakness in Internal Controls over the Financial Reporting Process** states in part that, *“In addition, the City should implement the applicable remedial actions as outlined in the Mayor’s August 24, 2006 responses to the Kroll Report.”*

In the City’s response to KPMG’s Recommendation under the heading, *Views of Responsible Officials*, it states that, *“We agree. The City recognizes the need for an improved financial reporting control framework and as such, continues to construct a better financial reporting process. **As part of this, the City has committed itself to implementing all applicable remediation actions as outlined in the Kroll Report.** Most notably, the City has begun the procurement process for a new financial accounting system (Enterprise Resource Planning System), implementation of this system will result in overhauling the vast majority of the City’s accounting practices.”*

The response provided (*Views of Responsible Officials*) however, fails to include the very important fact that the Mayor is modifying the implementation timeline for: **portions of Remediation #36** (“in connection with the annual audit of the financial statements of the City for the fiscal year ending June 30, 2008, conduct an audit of the City’s internal controls”) **portions of Remediation #58** (“a statement setting forth the City’s assessment of the effectiveness of the internal controls”) and **portions of Remediation # 59** (“a signed management report substantially in the form described for the Mayor and CFO”) as presented in the August 24, 2006 response to the Kroll Report. The *Views of Responsible Officials* response failed to include the fact that the timeline for Remediations #79 and #80 is being modified as well.

Status Report #5 states that, *“The audit of internal controls by an independent auditing firm is directly related to City management’s assessment of the effectiveness of internal controls. **City management believes audit of the City’s internal controls by a reputable independent auditing firm should not take place until the City’s new Enterprise Resource Planning (ERP) system has been implemented.** By the time the ERP system is implemented, the City should be current on audits of its CAFRs and should have sufficient resources to focus on internal controls over financial reporting.”*

**RECOMMENDATION:** The Audit Committee should review the City's responses (*Views of Responsible Officials*) to KPMG's **Internal Control Report**, and obtain clarification regarding management's response to **Item 2003-1**. This review and clarification should also include the timeline modifications to Kroll Remediation Items #79 and #80. The City Council Audit Committee and City Council, at a minimum, should insist upon the timely hiring of an independent auditing firm to assess the effectiveness of City's internal controls and not wait until after the implementation of the Enterprise Resource Planning system.

**ISSUE:** On February 16, 2007, SDCERS approved a City of San Diego Preservation of Benefit Plan that adds a \$22.8 million liability to the City of San Diego.

In the *Views of Responsible Officials* response to KPMG's **Internal Control Report, Item 2003-2, Violations of the Internal Revenue Code**, there is no mention of the most recent liability assumed by the City of San Diego from SDCERS – specifically, the new liability of \$22.8 million for the Preservation of Benefit Plan. The Preservation of Benefit Plan was adopted by SDCERS on February 16, 2007, as well as the approval of projected employer contributions to pay for the Preservation of Benefit Plan. The City's CFO is aware of this liability and it is estimated that the City will pay between \$400,000 - \$500,000 for Fiscal Year 2008. It is also my understanding that this liability will continue to grow.

**RECOMMENDATION:** Before City Council adoption of the Mayor's proposed Fiscal Year 2008 Budget, the Mayor/CFO should provide to the City Council Audit Committee and City Council a full and complete report on the Preservation of Benefit Plan. This report should include: (a.) whether the IRS has made a determination on the legality of the Preservation of Benefit Plan, and if so, when that determination was made and by whom; (b.) how to properly disclose this material fact to the public and secondary market and in the 2003 and subsequent CAFRs; (c.) whether this liability is in the Mayor's Five Year Financial Outlook and if there is a proposed revenue source to pay for this new liability.

**ISSUE:** The City of San Diego's Auditor & Comptroller website is inaccurate and outdated, and gives a false impression that the City of San Diego has an Auditor & Comptroller named John Torell.

Mr. John Torell, CPA and former City of San Diego Auditor & Comptroller, sent a letter of resignation to the Mayor on December 27, 2006. In it, Mr. Torell stated that he had committed to a January 15, 2007 start date for his new job in Santa Barbara. As of May 6, 2007 the following message still appeared on the City Auditor & Comptroller's website (see below and also attached). This message gives the false and misleading impression that John Torell is the City of San Diego's Auditor & Comptroller.

## Message from the City Auditor & Comptroller

As the chief fiscal officer of the City, the Auditor & Comptroller is responsible for providing oversight of City fiscal management through the City's Comprehensive Financial Report. We also assist management of the City in carrying out their responsibilities by providing professional audit services such as: attestation services, internal control reviews, performance reviews, fraud/loss, investigations and special projects. We are here to serve you.

### - John Torell, CPA, Esq., Auditor & Comptroller

**RECOMMENDATION:** Correct the San Diego's City Auditor & Comptroller website and homepage to provide accurate and updated information, including the fact the Mr. Torell is no longer employed as the City Auditor & Comptroller and that the City of San Diego does not have a City Auditor & Comptroller.

Attachment: City Auditor & Comptroller Homepage

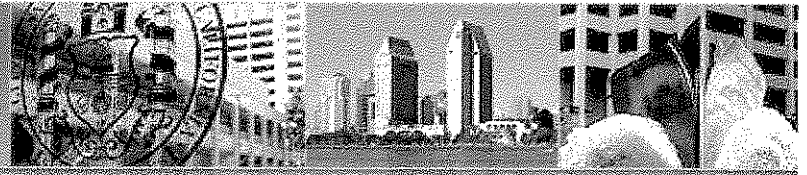
Cc: City Attorney, Michael Aguirre  
Deputy City Attorney, Mark Blake  
Independent Budget Analyst, Andrea Tevlin  
CFO, Jay Goldstone  
Deputy Comptroller, Greg Levin  
Mr. Stanley Keller, Independent Consultant



THE CITY OF SAN DIEGO

[Home](#) [Contact the City](#)[Business](#) [City Hall](#) [Community](#) [Departments](#) [Information](#) [Leisure](#) [Services A-Z](#) [Visiting](#) [Search](#)

## CITY AUDITOR &amp; COMPTROLLER

CITY AUDITOR &  
COMPTROLLER HOME[ABOUT US](#)[FINANCIAL  
REPORTS](#)[CAREERS](#)[CONTACT  
US](#)City Auditor  
& Comptroller

## What's New

**Comprehensive Annual Financial Report**, for Fiscal Year Ending June 30, 2003[FY03CAFR](#)  
(PDF: 4.9Mb)**Unclaimed Monies**

Are You Missing Something? NEW LIST! Updated as of 01/17/2007. Every day the City Auditor receives returned checks that were undeliverable by postal delivery.

- [Unclaimed Monies \(A-D\)](#)  
(PDF: 43K)
- [Unclaimed Monies \(E-K\)](#)  
(PDF: 41K)
- [Unclaimed Monies \(L-Q\)](#)  
(PDF: 41K)
- [Unclaimed Monies \(R-Z\)](#)  
(PDF: 47K)

Download the [Request for Unclaimed Monies Form](#) (PDF: 27K). Mail the properly completed and signed form to the address listed at the bottom of the form, in order to claim monies due you. Please allow 4 to 6 weeks processing time.

202 C Street, MS-6A  
San Diego, CA 92101  
[auditor@sandiego.gov](mailto:auditor@sandiego.gov)

## Message from the City Auditor &amp; Comptroller

As the chief fiscal officer of the City, the Auditor & Comptroller is responsible for providing oversight of City fiscal management through the City's Comprehensive Financial Report. We also assist management of the City in carrying out their responsibilities by providing professional audit services such as: attestation services, internal control reviews, performance reviews, fraud/loss, investigations and special projects. We are here to serve you.

- John Torell, CPA, Esq., Auditor & Comptroller

## Information

## Principles and Values

The City Auditor & Comptroller department has announced its new [Statement of Principles and Values](#) (PDF: 30K)

## Forms

Download forms

- [Request for Unclaimed Monies](#)  
(PDF: 27K)
- [Affidavit to Obtain Duplicate Check](#) (PDF: 201K)

## Departmental Update

Our department is currently going through a reorganization effort. [View the current information regarding the effort.](#)

## 2007 Internal Controls Report

The 2007 Internal Controls Report is available by clicking [here](#).  
(PDF: 641K)

## FAQ

- [Where do I pay my taxes?](#)
- [I sent you an invoice where is my check?](#)
- [More...](#)

## CAREERS

With the City Auditor & Comptroller Department

## FORMS

Download Forms

## Organization Chart

## Financial Reports

[City Auditor & Comptroller Home](#) [About Us](#) [Financial Reports](#) [Careers](#) [Contact Us](#) [Top of Page](#)

[Site Map](#) [Privacy Notice](#) [Disclaimers](#)

[Home](#) [Business](#) [City Hall](#) [Community](#) [Departments](#) [Information](#) [Leisure](#) [Services A-Z](#) [Visiting](#)  
[Search](#) [Site Map](#) [Contact the City](#) [Privacy Notice](#) [Disclaimers](#)